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Soviets turning to Western banks for loans with no strings attached

By Karen Riley
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Pinched by declining export revenues, the Soviet Union is looking increasingly to Western commercial banks for money.

At the same time, many of the major banks in the non-communist world are eager to supply hard currency to Moscow at attractive rates. The loans are usually not tied to a particular transaction and can be used for anything from building weapons to conducting the war in Afghanistan.

Last month, for example, First Chicago National Bank was the lead agent on a $200 million syndicated loan to the Soviet Foreign Trade Bank. The loan was priced 1/8 of 1 percent above the London InterBank rate, a rate so low that many banks would have trouble making any profit on it, banking sources said.

"I doubt that any of First Chicago's other customers, from struggling farmers right up to prime corporate borrowers, could get this kind of deal from their bank," said Sen. Jake Garn, Utah Republican, who has introduced legislation to give the president authority to control the transfer of money from the United States to the Soviet Union.

The Chicago bank was paid a fee for acting as agent for the loan. Richard Mueller, an analyst with the Chicago securities firm of Duff & Phelps, said First Chicago probably got the standard 0.20 percent to 0.50 percent fee — as much as $1 million.

The loan was First Chicago's latest in a series of loans to the Soviet Union beginning in 1985. The loan from First Chicago didn't come from American depositors, but was raised outside the United States to skirt the Johnson Debt Default Act, a Depression-era law that bars American banks from making loans to nations such as the Soviet Union that remain in default with this country, said Judy Shelton, a fellow with the Hoover Institute in Palo Alto, Calif.

The loan was for "fostering civil exports," said Anthony Zehnder, spokesman for First Chicago.

But the loan is not tied to a specific purpose, he said, and theoretically could be used for anything.

As the largest bank in the wheat belt, First Chicago is positioned to be the lead lender for grain sales between the United States and the Soviet Union, banking sources note. The bank also hopes to get a foot in the door if overall trade opportunities between the two countries blossom.

Like most banks that make syndicated loans to the Soviets, First Chicago has no trouble signing on other banks because the Soviet Union is still considered a good credit risk and its loans cost less to process than others.

Banks lend to Moscow in two ways: through syndicated loans, which are repackaged into small amounts and resold, and through bankers acceptance facilities, similar to letters of credit. In addition, there is some interbank lending on an estimated $5 billion of Western deposits in the seven Soviet banks that operate in non-communist nations, according to Roger W. Robinson, president of RWR Inc., an economics consulting firm in Washington.

William J. McDonough, vice chairman of First Chicago, told a Senate hearing in 1985 that the main attraction of Soviet loans was "the fees we earned for our activities as an investment banker."

First Chicago has made loans to other Soviet bloc nations. It was among the first Western banks to open an office in Poland. And Federal Reserve Board documents indicate the bank has loaned money to Hungary and Czechoslovakia.

Its latest loans have caused "some eyebrow-raising" in Chicago, Mr. Mueller said.

Other banks have also been active in lending to Moscow.

Last fall, the Banque Nationale de Paris syndicated a $300 million loan to the Soviets that carried a rate of 1/8 of 1 percent over the London Interbank rate for part the 8-year loan period.

Credit Lyonnais loaned $100 million to Moscow late last year.

And the Soviet Union is reported to have negotiated a loan with Kuwait, according to a banking source.

All told, Moscow borrowed about $6 billion from the West in 1985 and $6.4 billion in 1986, according to joint estimates from the CIA and the Defense Intelligence Agency. The Soviet Union has set a goal of borrowing $5 billion in 1987, according to Mr. Garn.

About 60 percent of the money will come from commercial banks, most of them outside the United States.

Behind the big borrowing binge is a steep decline in Soviet export earnings. Oil and gas exports make up 60 percent of the Soviet Union's hard currency earnings. But with falling oil prices, Moscow's earnings are down $8 billion to $9 billion.

In addition, Western nations, which once supplied Moscow with half its outside loans, have been cutting back on official trade credits since 1982. Official trade credits now supply Moscow with only 44 percent of its total financing.

These trade credits could decline even further in the future because the United States and other industrialized countries recently agreed to prohibit any interest-rate subsidies on their loans or guarantees to the Soviet Union.

The difference has been "more than made up by increased borrowing from commercial banks," said Richard Neu of the Rand Corp. in California.

The numbers are uncertain but data compiled by the Organization for Economic Cooperation and Development (OECD) and the Bank for International Settlements indicate that Soviet debt to commercial banks climbed from $19.3 billion in June 1985 to $26.8 billion in June 1986.

Supplemental third-quarter 1986 data to be released shortly are likely to show a further increase, according to Mr. Neu.

Soviet financial dealings are receiving more scrutiny in Congress and elsewhere.

Sen. William Proxmire, Wisconsin Democrat and chairman of the Senate Banking Committee, is co-sponsoring Mr. Garn's Financial Export Control Act, an expanded version of a 1985 bill.

The bill, which has support on both sides of the aisle, would give the president authority to control the transfer of money from the United States to countries subject to national security export controls.

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"The Soviet ability to obtain the sensitive goods and technology from the West that are turned against us in Soviet weapon systems is directly related to their ability to obtain hard currency," Mr. Garn said in a March 19 speech on the Senate floor.

The Reagan administration, which opposed a similar bill before, is expected to oppose this one, as well, in the interest of U.S.-Soviet relations.

Meanwhile, a report on Soviet financial dealings is waiting to be cleared by the Joint Economic Committee.

Mr. Neu of Rand recently completed a similar study for the Defense Department. That study hasn't been released yet, either.

"Moscow's external debt buildup over the next three to five years may make the U.S.S.R. a somewhat less appealing credit risk, particularly if Soviet hard currency export opportunities remain as narrow as they are today," Mr. Robinson said in a recent interview published in Human Events.

Indeed, the OECD recently forecast that the Soviet Union could become a high-debt country.

The main Soviet lenders are West European and Japanese banks. U.S. involvement amounts to "peanuts," said Jan Vanous of the PlanEcon research firm in Washington. American banks stopped lending to the Soviet Union after it invaded Afghanistan in December 1979 and didn't begin again until 1985.